

Report of the Auditor-General to the Eastern Cape Provincial Legislature and the council on Sundays River Valley Local Municipality

Report on the financial statements

Introduction

1. I was engaged to audit the financial statements of the Sundays River Valley Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget information with actual information for the year then ended as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa (Act No. 10 of 2014) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with International Standards on Auditing. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Property, plant and equipment

4. The municipality did not account for its property, plant and equipment in accordance with *GRAP 17: Property, plant and equipment* in the following instances:
 - Property, plant and equipment disclosed in the statement of financial position and note 10 to the financial statements did not include all assets that belong to the municipality. As a result property, plant and equipment and accumulated surplus was understated by R219,6 million (2013-14: R219,6 million).

- Furthermore, the municipality included the assets where the risks and rewards incidental to ownership of the assets had not transferred to the municipality for infrastructure assets as disclosed in the statement of financial position and note 10 to the financial statements. Consequently infrastructure assets and revenue from non-exchange transactions were overstated by R39,7 million (2013-14: R27,8 million).
5. In addition sufficient and appropriate evidence was not available to support property, plant and equipment disclosed in the statement of financial position and note 10 to the financial statements. The municipality did not have adequate systems and processes in place to account for assets. I was unable to confirm the property, plant and equipment by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to property, plant and equipment disclosed at R493,9 million (2013-14: R481,5 million) in the statement of financial position and note 10 to the financial statements.

Irregular Expenditure

6. The municipality did not have adequate systems in place to identify and disclose all irregular expenditure incurred during the year as required by section 125(2)(d)(i) of the MFMA. The irregular expenditure disclosed in note 38 to the financial statements is understated in respect of amounts incurred during the year that were identified during the audit process. Due to the lack of systems and sufficient appropriate audit evidence for all awards, it was impracticable to determine the full extent of the understatement of irregular expenditure, and it was not possible to confirm this by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to the irregular expenditure disclosed at R72,3 million (2013-14: R84,5 million).

Investment property

7. The municipality did not recognise all property held to earn rental income or for capital appreciation as investment property in accordance with *GRAP 16: Investment Property*. This was due to the municipality not having adequate systems in place to account for all its investment property. Consequently investment property disclosed in the statement of financial position and in note 7 to the financial statements was understated by R20,6 million (2013-14: R20,6 million) and the accumulated surplus was understated by the same amount.
8. In addition sufficient and appropriate evidence was not available to support investment property disclosed in the statement of financial position and note 7 to the financial statements. This was due to a lack of systems and processes in place at the municipality. I was unable to confirm the investment property by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to investment property disclosed at R22,8 million (2013-14: R22,8 million).

Revenue from exchange transactions

9. The municipality did not measure revenue at the fair value of the consideration received or receivable in accordance with *GRAP 9: Revenue from exchange transactions*. This was due to management not having systems to account for revenue and ensure that it was completely recorded. Consequently revenue and receivables from exchange transactions as disclosed in note 19 and note 5 to the financial statements was understated by R11,3 million.

10. In addition sufficient and appropriate evidence was not available to support revenue from exchange transactions as presented in the statement of financial performance. This was due to a lack of systems and processes in place at the municipality. I was unable to confirm the revenue from exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to revenue from exchange transactions disclosed at R69,6 million in the statement of financial performance.

Revenue from non-exchange transactions

11. The municipality did not recognise revenue in terms of *GRAP 23: Revenue from non-exchange transactions* as items that did not meet the definition of revenue were included in the financial statements, revenue was not measured at the fair value of the consideration received or receivable and there were no systems to ensure that revenue was completely accounted for. Consequently revenue from non-exchange transactions as disclosed in note 19 to the financial statements is overstated by R6,3 million (2013-14: understated by R3,2 million), receivables from non-exchange transactions was understated by R4 million (2013-14: Understated by R3.2 million) and PPE was overstated by R10,2 million.
12. In addition sufficient and appropriate evidence was not available to support revenue from non-exchange transactions presented in the statement of financial performance. This was due to a lack of systems and processes in place at the municipality. I was unable to confirm the revenue from non-exchange transactions by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to revenue from non-exchange transactions disclosed at R137,9 million (2013-14: R88,1 million) in the statement of financial performance and note 22 to the financial statements.

Commitments

13. The municipality did not have an adequate and complete contract management system in place for the identification and recognition of contracted commitments and did not include commitments of at least R8 million in the amounts disclosed in note 33 to the financial statements. Due to the lack of adequate systems in place, it was impracticable to determine the full extent of the understatement of commitments as disclosed.
14. In addition sufficient and appropriate evidence was not available to support commitments disclosed in note 33 to the financial statements. This was due to a lack of systems and processes in place at the municipality. I was unable to confirm the commitments by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to commitments as disclosed at R37,6 million (2013-14: R28,9 million).

Receivables from exchange and non-exchange transactions

15. Sufficient and appropriate audit evidence was not available to support receivables from non-exchange transactions and receivables from exchange transactions as disclosed in note 4 and 5 to the financial statements. This was due to a lack of systems and processes in place at the municipality. I was unable to confirm this balance by alternative means. Consequently, I was unable to determine whether any further adjustments to receivables from non-exchange transactions and exchange transactions disclosed at R3,7 million and R19,2 million respectively were necessary.

Depreciation

16. The municipality did not consistently apply the accounting policy for depreciation in accordance with GRAP 3: *Accounting policies, changes in accounting estimates and errors*. A different policy to what was disclosed in the financial statements was applied in calculating the depreciation for the year. Consequently depreciation was understated by R2,8 million (2013-14: overstated by R6,4 million) and PPE was overstated by the same amount.

General expenditure

17. The municipality did not recognise all expenses that met the definition of expenditure in accordance with GRAP 1: *Presentation of financial statements*. The municipality did not have adequate processes in place to identify and correctly recognise all expenditure. Consequently general expenditure and payables from exchange transactions as disclosed in 31 and note 13 to the financial statements was understated by R3,4 million (2013-14: R11,9 million).
18. In addition sufficient and appropriate evidence was not available to support expenditure transactions disclosed at R39,4 million in note 31 to the financial statements. This was due to a lack of systems and processes in place at the municipality. I was unable to confirm the amount by alternative means. Consequently, I was unable to determine whether any further adjustment to general expenditure was necessary.

Bulk purchases

19. The municipality did not ensure that bulk purchases incurred met the definition of expenditure in accordance with GRAP 1: *Presentation of financial statements*. There were inadequate processes in place to ensure that bulk purchases were appropriately recorded. Consequently bulk expenditure and payables from exchange transactions as disclosed in note 30 and 13 to the financial statements is overstated by R5,9 million (2013-14: understated by R1,5 million).

Employee Costs

20. The municipality did not recognise expenses that met the definition of expenses in accordance with GRAP 1: *Presentation of financial statements*. The underlying records did not agree to the amounts disclosed in note 24 to the financial statements. The municipality did not have adequate processes in place to identify and correctly recognise employee related expenditure appropriately. Employee costs as disclosed in note 24 to the financial statements was overstated and receivables from non-exchange transactions as disclosed in note 4 to the financial statements was understated by R3,6 million.
21. In addition sufficient and appropriate evidence was not available to support employee costs of R41,1 million as disclosed in the statement of financial performance and in note 24 to the financial statement. Supporting documentation was not provided for overtime, wages, allowances, journals and third party payments. I was unable to confirm the transactions by alternative means. Consequently, I was unable to determine whether any further adjustments to employee costs were necessary.

Impairment Losses

22. The municipality did not account for the impairment losses in accordance with the requirements of *GRAP 104: Financial Instruments* as they did not follow their accounting policy in calculating these losses. As a result, the impairment losses disclosed in note 27 to the financial statements was understated by R10,9 million (2013-14: R3,3 million) while receivables from exchange transactions and non-exchange transactions combined were overstated by the same amount.
23. Sufficient and appropriate evidence was not available to support impairment losses disclosed at R42,8 million on the statement of financial performance and in note 27 to the financial statements. This was due to the municipality not having adequate document management processes in place. I was unable to confirm the amount by alternative means. Consequently, I was unable to determine whether any further adjustments to impairment losses were necessary.

Employee benefit obligation

24. Sufficient and appropriate evidence was not available to support employee benefits disclosed in note 17 to the financial statements. This was due to the municipality not having adequate document management processes in place. I was unable to confirm the balance by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to employee benefits obligation disclosed at R3,5 million (2013-14: R3,4 million).

Payables from exchange transactions

25. The municipality did not include all outstanding amounts meeting the definition of a liability as per *GRAP 1: Presentation of financial statements* in the financial statements. The municipality did not accrue for all payables for which goods or services had already been received at year end. Consequently, payables from exchange transactions as disclosed in the statement of financial position and note 13 to the financial statements was understated by R18,8 million (2013-14: R487 003), expenditure as disclosed in the statement of financial performance was understated by R20,7 million (2013-14: Overstated by R11 563) and employee cost as disclosed in note 24 to the financial statements was overstated by R1,9 million (2013-14: Understated by 498 566).
26. In addition sufficient and appropriate evidence was not available to support payables from exchange transactions disclosed in note 13 to the financial statements. This was due to the municipality not having adequate document management processes in place. I was unable to confirm the balance by alternative means. Consequently, I was unable to determine whether any further adjustments were necessary to payables from exchange transactions disclosed at R4,5 million (2013-14: R4,2 million).

Cash flow statement

27. Sufficient and appropriate evidence was not available to support the cash flow statement disclosed in the financial statements as the municipality did not have adequate document management processes in place. I was unable to confirm the cash flow statement by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the cash flow statement as disclosed in the financial statements.

VAT Payable

28. Sufficient and appropriate evidence was not available to support the VAT payable disclosed in the statement of financial position and note 14 to the financial statements. This was due to the municipality not having adequate document management processes in place. I was unable to confirm the VAT payable by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to VAT payable disclosed at R6,2 million (2013-14: R4,1 million).

Unspent Conditional Grants

29. The municipality did not include all outstanding amounts meeting the definition of a liability as per *GRAP 1: Presentation of financial statements* in the financial statements. Management did not carry forward the closing balances from prior year. Consequently, unspent conditional grants and revenue from non-exchange transactions as disclosed in the statement of financial position and note 16 and the statement of financial performance and note 22 to the financial statements was understated by R5,7 million (2013-14: R2,8 million).
30. In addition sufficient and appropriate evidence was not available to support unspent conditional grants disclosed in note 16 to the financial statements. This was due to the municipality not having adequate document management processes in place. I was unable to confirm the balance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to unspent conditional grants disclosed at R7,5 million (2013-14: R400 000) per note 16 to the financial statements.

Finance Lease obligations

31. Sufficient and appropriate evidence was not available to support the finance lease obligation disclosed in the statement of financial position and note 12 to the financial statements. This was due to the municipality not having adequate document management processes in place. I was unable to confirm the balance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to finance lease obligation disclosed at R2,8 million (2013-14: R1,8 million).

Unauthorised Expenditure

32. The municipality did not have adequate systems in place to identify and disclose all unauthorised expenditure incurred during the year as required by section 125(2)(d)(i) of the MFMA. Unauthorised expenditure of R9,7 million was identified through the audit process because the municipality did not have sufficient monitoring controls to ensure all unauthorised expenditure was recognised and disclosed. As a result, unauthorised expenditure as disclosed in note 37 to the financial statements is understated by R9,7 million (2013-14: R40,8 million).

Fruitless and wasteful expenditure

33. The municipality did not have adequate systems in place to identify and disclose all fruitless and wasteful expenditure incurred during the year as required by section 125(2)(d)(i) of the MFMA. Additional fruitless and wasteful expenditure of R4 million was identified through the audit process that was not disclosed in the financial statements. Consequently fruitless and wasteful expenditure disclosed in note 39 to the financial statements was understated by R4 million.

Statement of changes in Net assets

34. The municipality did not present the statement of comparison of changes in net assets in accordance with GRAP 1: Presentation of financial statements. The statement did not cast correctly and an understatement of R4,4 million was identified for accumulated surplus disclosed as at 1 July 2013.

Corresponding figures

Adjustments to corresponding figures

35. Sufficient and appropriate evidence was not available to support the changes made to the comparative information disclosed in note 42 to the financial statements. This was due to the municipality not having adequate document management processes in place. I was unable to determine whether any further adjustments to the below prior period adjustments affecting the corresponding figures as disclosed in note 42 to the financial statements were necessary:

- Depreciation expense of R6,1 million.
- Loss of disposal of assets of R2,5 million
- Cash and cash equivalents of R6,6 million
- Opening Accumulated Surplus or Deficit of R91,7 million
- Bank overdraft of R6,7 million
- Payables from exchange transactions of R9,4 million
- Unspent conditional grants of R2,7 million
- Receivables from non-exchange of R1,5 million
- Receivables from exchange of R1,9 million
- Finance costs of R1,8 million
- General expenditure of R7,9 million

36. In addition the correction of errors reflected at R110,3 million in the statement of changes in net assets did not agree to note 42 to the financial statements and a difference of R18,7 million was identified.

Material misstatements in the corresponding figures

37. During the audit of the 2013-14 financial year, I identified the following misstatements that are still included in the corresponding figures disclosed in the 2014-15 financial statements:

- Repairs and maintenance reflected at R6,4 million in note 29 to the financial statement was overstated by R5,4 million and accumulated surplus was overstated by the same amount.
 - Receivables from non-exchange transactions and exchange transactions as reflected at R2,2 million and at R8 million in note 4 and note 5 to the financial statements respectively, was understated by a combined amount of R5,8 million. Consequently, revenue from exchange transactions reflected at R45,2 million in note 19, revenue from non-exchange transactions reflected at R13,9 million in note 22 and cash and cash equivalents reflected at R7,1 million in note 6 to the financial statements was overstated by R500 000, 3,1 million and R2,2 million respectively.
38. In addition, I was also unable to obtain sufficient appropriate audit evidence for the following elements included in the 2013-14 financial statements. During the current year, I was again not provided with the evidence required to substantiate these transactions and balances. I was thus unable to confirm by alternative means, or determine whether adjustments were required to:
- Bulk expenditure disclosed at R14,7 million in note 30 to the financial statements.
 - The cash flow statement included in the financial statements.
 - Other receivables from non-exchange disclosed at R700 000 million in note 4 to the financial statements.

Aggregation of immaterial uncorrected corresponding misstatements

39. The financial statements as a whole was materially misstated due to the cumulative effect of numerous individually immaterial uncorrected misstatements in the following corresponding elements making up the 2013-14 and the notes to the financial statements:
- Cash and cash equivalents reflected as R7,1 million in note 6 to the financial statements was overstated by R2,3 million and receivables from exchange and non-exchange reflected as R19,2 million in note 5 and R3,7 million in note 4 was understated by the same amount.
 - Borrowings reflected as R4,4 million in note 11 to the financial statements was understated by R1,3 million and finance costs reflected as R2,2 million in note 28 was overstated by R391 697, general expenditure reflected as R35,7 million in note 31 was understated by R1 million, unspent conditional grants reflected as R380 498 in note 16 was overstated by R54 182 and income from agency services reflected as R1,1 million in the statement of financial performance was overstated by R651 260.
40. My audit opinion on the financial statements for the period ended 30 June 2014 was modified accordingly. My opinion on the current period's financial statements is also modified because of the possible effect of these matters on the comparability of the current period's figures.

Disclaimer of opinion

41. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Emphasis of matter paragraphs

42. The following emphasis of matter paragraphs will be included in our auditor's report to draw the users' attention to matters presented or disclosed in the financial statements:

Restatement of corresponding figures

43. As disclosed in note 42 to the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of errors only corrected during the year ended 30 June 2015 that existed in the financial statements at, and for the year ended 30 June 2014.

Material impairment losses

44. As disclosed in note 27 to the financial statements, a material loss to the amount of R 42.5 million was incurred as a result of irrecoverable trade debtors. This is due to poor debt collection processes.

Additional matters

45. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited supplementary schedules

46. The supplementary annexures set out on pages XX to XX do not form part of the financial statements and are presented as additional information. We have not audited these schedules and accordingly we do not express an opinion thereon.

Report on other legal and regulatory requirements

47. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report, compliance with legislation and internal control. The objective of my tests was to identify reportable findings as described under each subheading, but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

48. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected objectives presented in the annual performance report (APR) of the municipality for the year ended 30 June 2015:
- Basic service delivery and infrastructure development on pages x to x
 - Community and social services on pages x to x
 - Local economic development on pages x to x
49. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
50. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned objectives. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
51. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
52. The material findings in respect of the selected objectives are as follows:

Basic service delivery and infrastructure development

Usefulness of reported performance information

53. Section 41(c) of the Municipal Systems Act (MSA) requires the integrated development plan (IDP) to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 80% of the reported objectives, 24% of the reported indicators and 29% of the reported targets were not consistent with those in the IDP and Service delivery and implementation plan (SDBIP). This was due to lack of established processes and systems.
54. Section 54(1)(c) of the MFMA determines that the SDBIP adopted by the municipal council may be amended only if the council approves an adjustments budget. Changes to the SDBIP in the year have to be made in accordance with the process as prescribed per section 28 of the MFMA. Material changes were made to the objectives and targets in the APR, without following the process as prescribed in section 28 of the MFMA and without adoption by the municipal council. This was due to lack of monitoring and review of the APR by the relevant oversight bodies.
55. Performance targets should be specific in clearly identifying the nature and required level of performance and should also be measurable, as required by the FMPPI. A total of 80% of the targets were not specific and measurable. This was because management were not aware of and were not adequately trained in the requirements of the FMPPI.
56. Performance indicators should be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use, as required by the FMPPI. A total of 88% of performance indicators were not well defined. This was

because management were not aware of and were not adequately trained in the requirements of the FMPPI.

57. The processes and systems that produced the indicator should be verifiable, as required by the FMPPI. All of the indicators were not verifiable. This was because management was not aware of and was not adequately trained in the requirements of the FMPPI.
58. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. A total of 63% of the indicators did not relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives as per the IDP. This was because proper performance planning and management practices had not been developed and implemented to provide for the development of performance indicators and targets included in the APR.

Reliability of reported performance information

59. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and the auditee's records not permitting the application of alternative audit procedures.
60. The fact that proper indicator definitions were not used to predetermine the evidence and method of calculation for actual achievements also contributed to evidence being collected in an inconsistent manner and resulted in a lack of suitable evidence being collected to support the reported performance.

Community and social services

Usefulness of reported performance information

61. Section 41(c) of the Municipal Systems Act requires the IDP to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 29% of the reported objectives and 57% of the reported targets were not consistent with those in the approved IDP and SDBIP. This was due to lack of established processes and systems.
62. Section 54(1)(c) of the MFMA determines that the SDBIP adopted by the municipal council may be amended only if the council approves an adjustments budget. Changes to the SDBIP in the year have to be made in accordance with the process as prescribed per section 28 of the MFMA. Material changes were made to the objectives and targets in the APR, without following the process as prescribed in section 28 of the MFMA and without adoption by the municipal council. This was due to lack of monitoring and review of the APR by the relevant oversight bodies.
63. Performance targets should be specific in clearly identifying the nature and required level of performance and should also be measurable as required by the FMPPI. A total of 44% of the targets were not specific and measurable. This was because management was not aware of and was not adequately trained in the requirements of the FMPPI. There is also a lack of proper systems, processes and technical indicator descriptions.

64. Performance indicators should be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use, as required by the FMPPI. A total of 72% of performance indicators were not well defined. This was because management was not aware of and was not adequately trained in the requirements of the FMPPI. There was also a lack of proper systems, processes and technical indicator descriptions.
65. The processes and systems that produced the indicator should be verifiable, as required by the FMPPI. All of the indicators were not verifiable. This was because management were not aware of and were not adequately trained in the requirements of the FMPPI.
66. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. A total of 44% of the indicators did not relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives as per the IDP. This was due to inadequate performance planning and management practices had not been developed and implemented to provide for the development of performance indicators and targets included in the APR.

Reliability of reported performance information

67. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and the auditee's records not permitting the application of alternative audit procedures.
68. The fact that proper indicator definitions were not used to predetermine the evidence and method of calculation for actual achievements also contributed to evidence being collected in an inconsistent manner and resulted in a lack of suitable evidence being collected to support the reported performance.

Local economic development

Usefulness of reported performance information

69. Section 41(c) of the Municipal Systems Act requires the IDP to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 60% of the reported objectives were not consistent with those in the approved IDP and SDBIP. This was due to lack of established processes and systems.
70. Section 54(1)(c) of the MFMA determines that the SDBIP adopted by the municipal council may be amended only if the council approves an adjustments budget. Changes to the SDBIP in the year have to be made in accordance with the process as prescribed per section 28 of the MFMA. Material changes were made to the objectives in the APR, without following the process as prescribed in section 28 of the MFMA and without adoption by the municipal council. This was due to lack of monitoring and review of the APR by the relevant oversight bodies.
71. Performance targets should be specific in clearly identifying the nature and required level of performance and should be measurable as required by the FMPPI. All of the targets were not specific and measurable. This was because management were not aware of

and were not adequately trained in the requirements of the FMPPI. There was also a lack of proper systems, processes and technical indicator descriptions.

72. Performance indicators should be well defined by having clear definitions so that data can be collected consistently and is easy to understand and use, as required by the FMPPI. In addition, processes and systems that produced the indicator should be verifiable, as required by the FMPPI. All of the performance indicators were not well defined or verifiable. This was because management were not aware of and were not adequately trained in the requirements of the FMPPI. There was also a lack of proper systems, processes and technical indicator descriptions.
73. The FMPPI requires indicators to relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives. A total of 75% of the indicators did not relate logically and directly to an aspect of the auditee's mandate and the realisation of strategic goals and objectives as per the IDP. This was because proper performance planning and management practices had not been developed and implemented to provide for the development of performance indicators and targets included in the APR.

Reliability of reported performance information

74. The FMPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information. This was due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information and the auditee's records not permitting the application of alternative audit procedures.
75. The fact that proper indicator definitions were not used to predetermine the evidence and method of calculation for actual achievements also contributed to evidence being collected in an inconsistent manner and resulted in a lack of suitable evidence being collected to support the reported performance.

Additional matters

76. I draw attention to the matters below. My opinion is not modified in respect of this matter.

Achievement of planned targets

77. Refer to the annual performance report on pages x to x for information on the achievement of the planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information for the selected objectives reported in paragraphs 46 to 74 of this report.

Adjustment of material misstatements

78. I identified material misstatements in the annual performance report submitted for auditing on the reported performance information for infrastructure investment, economic development and community and social services. As management subsequently corrected only some of the misstatements, I identified material findings on the usefulness and reliability of the reported performance information.

Unaudited supplementary schedules

79. The supplementary information set out on pages XX to XX does not form part of the annual performance report and is presented as additional information. I have not audited these schedules and, accordingly, I do not report thereon.

Compliance with legislation

80. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My material findings on compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows.

Strategic planning and performance management

81. The adopted IDP did not reflect and identify a financial plan and the key performance indicators and targets, as required by sections 26 and 41 of the MSA, as well as Municipal planning and performance management regulation 2(1)(c)
82. The local community was not afforded the opportunity to comment on the final draft of the IDP before adoption, as required by section 42 of the MSA and Municipal planning and performance management regulation 9, 13(1), 13(4)(c) and 15(3).
83. The municipality did not give effect to its integrated development plan and conduct its affairs in a manner which was consistent with its integrated development plan, as required by section 36 of the MSA, section 21(2)(a) of the MFMA and Municipal planning and performance management regulation 6.
84. The performance management system did not provide for policies and procedures to take steps of improvement where performance targets were not met, as required by section 41 (1)(d) of the MSA.
85. Key performance indicators, including input, output and outcome indicators, in respect of each of the development priorities and objectives were not set out in the IDP, as required by section 41(1)(a) of the MSA and the Municipal planning and performance management regulation 1 and 9(1)(a).
86. The KPIs set by the municipality in the amended SDBIP did not include indicators on percentage of households with access to basic level of water, electricity and solid waste removal as required by section 43(2) of the MSA and the Municipal planning and performance management regulation 10(a).
87. Measurable performance targets for the financial year were not set in the IDP, for each of the key performance indicators and with regard to each of the development priorities or objectives, as required by section 41(1)(b) of the MSA and the Municipal planning and performance management regulations 12(1) and 12(2)(e).
88. The SDBIP for implementing the municipality's delivery of municipal services and annual budget did not indicate projections for each month of the revenue to be collected, by source and the operational and capital expenditure, by vote.
89. The performance management system was not in line with the priorities, objectives, indicators and targets contained in its integrated development plan, did not relate to the employee's performance management processes and did not link to the integrated

development planning processes as required by section 38(a) of the MSA and Municipal planning and performance management regulation 7(2).

90. The performance management system and related controls were inadequate as it did not describe and represent the processes of performance planning, monitoring, measurement, review, reporting, improvement, and how it is conducted, organised and managed, including determining the roles of the different role-players, as required by sections 38 of the MSA and regulation 7 of the Municipal planning and performance management regulations.
91. The performance of the municipality were not assessed during the first half of the financial year, as required by section 72(1)(a)(ii) of the MFMA.

Annual reports and Annual Financial Statements

92. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors were not adequately corrected and the supporting records could not be provided subsequently which resulted in the financial statements receiving a disclaimer of opinion.
93. The annual performance report for the year under review did not include
 - the performance of each external services provider, and
 - a comparison of the performance and set targets of the previous financial year as required by section 46(1)(a) and 46(1)(b) of the MSA.
94. The oversight report, containing comments on the annual report, was not adopted by council within two months from the date on which the 2013/14 annual report was tabled, as required by section 129(1) of the MFMA.

Consequence management

95. Unauthorised, Irregular, Fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.
96. Council certified irregular expenditure as irrecoverable without having conducted an investigation to determine the recoverability of the expenditure, in contravention of section 32(2)(a)(ii) of the MFMA.
97. Sufficient appropriate audit evidence could not be obtained to confirm that unauthorised, irregular and fruitless and wasteful expenditure was always recovered from the liable person, as required by section 32(2) of the MFMA.

Audit Committee

98. The audit committee did not submit, at least twice during the financial year, an audit report on the review of the performance management system to the council, as required by Municipal planning and performance management regulation 14(4)(a)(iii).

Revenue management

99. A credit control and debt collection policy was not maintained and implemented, as required by section 96(b) of the Municipal Systems Act and section 62(1)(f)(iii) of the MFMA
100. An adequate management, accounting and information system which accounts for revenue, debtors and receipts of revenue was not in place, as required by section 64(2)(e) of the MFMA.
101. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
102. A policy was not implemented for the levying of rates on rateable property within the municipality, as required by section 3(1) of the Property Rates Act and section 62(1)(f)(ii) of the MFMA.

Expenditure management

103. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
104. Payments were made from the municipality's bank account without the approval of the accounting officer or the chief financial officer or a properly authorised official, as required by section 11(1) of the MFMA.
105. An effective system of expenditure control, including procedures for the approval and authorisation of payment of funds, was not in place, as required by section 65(2) (a) of the MFMA.
106. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, accounted for creditors and accounted for payments made as required by section 65(2)(b) of the MFMA.
107. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure, fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Conditional grants and transfers

108. Sufficient appropriate evidence could not be obtained that the Municipal Infrastructure Grant allocation and the Local Government Financial Management Grant was spent in accordance with the applicable grant framework, in contravention of section 17(1) of the DoRA.
109. The municipality did not evaluate its performance in respect of programmes or functions funded by the Local Government Financial Management Grant allocation, as required by section 12(5) of the DoRA.

Procurement and contract management

110. Sufficient appropriate audit evidence could not be obtained that all contracts were awarded in accordance with the legislative requirements and a procurement process

which is fair, equitable, transparent and competitive, as management indicated that these were burnt in the fire in the first quarter of the year.

111. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) & (c).
112. Sufficient appropriate audit evidence could not be obtained that goods and services of a transaction value above R500 000 were procured by means of inviting competitive bids, as required by SCM regulation 19(a).
113. Sufficient appropriate audit evidence could not be obtained that bid specifications for procurement of goods and services through competitive bids were drafted in an unbiased manner that allowed all potential suppliers to offer their goods or services, as per required by SCM regulation 27(2)(a).
114. Sufficient appropriate audit evidence could not be obtained that bid specifications were drafted by bid specification committees which were composed of one or more officials of the municipality as required by SCM regulation 27(3).
115. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding were advertised for a required minimum period of days, as required by SCM regulation 22(1) & 22(2).
116. Sufficient appropriate audit evidence could not be obtained that bids were evaluated by bid evaluation committees which were composed of officials from the departments requiring the goods or services and at least one SCM practitioner of the municipality as required by SCM regulation 28(2).
117. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to bidders based on points given for criteria that were stipulated in the original invitation for bidding and quotations, as required by SCM Regulations 21(b) and 28(1)(a) and Preferential Procurement Regulations.
118. Sufficient appropriate audit evidence could not be obtained that bid adjudication was always done by committees which were composed in accordance with SCM regulation 29(2).
119. Sufficient appropriate audit evidence could not be obtained that awards were made to bidders recommended by the bid evaluation committee except where ratified by the accounting officer, as required by SCM regulation 29(5)(b).
120. Sufficient appropriate audit evidence could not be obtained that Councillors of the municipality did not participate in committees evaluating or approving tenders or did not attend meetings of committees evaluating or approving tenders, in contravention of section 117 of the MFMA
121. The preference point system was not applied in all procurement of goods and services above R30 000 as required by section 2(a) of the Preferential Procurement Policy Framework Act and SCM regulation 28(1) (a).
122. Sufficient appropriate audit evidence could not be obtained that contracts were awarded to suppliers based on preference points that were allocated and calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.

123. Quotations were not awarded to bidders based on preference points that were allocated and or calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.
124. Sufficient appropriate audit evidence could not be obtained that contracts and quotations were awarded to bidders that scored the highest points in the evaluation process, as required by of section 2(1) (f) of Preferential Procurement Policy Framework Act.
125. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
126. Sufficient appropriate audit evidence could not be obtained that construction contracts were awarded to contractors that were registered with the Construction Industry Development Board (CIDB) and qualified for the contract in accordance with section 18(1) of the CIDB Act and CIDB regulations 17 and 25(7A)
127. Construction projects were not always registered with the CIDB, as required by section 22 of the CIDB Act and CIDB regulation 18.
128. Sufficient appropriate audit evidence could not be obtained that contracts were only extended or modified after tabling the reasons for the proposed amendment in the council of the municipality as required by section 116(3) of the MFMA.
129. Sufficient appropriate audit evidence could not be obtained that all extension or modification to contracts were approved by a properly delegated official, as required by SCM Regulation 5.
130. The performance of contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.
131. The contract performance and monitoring measures and methods were insufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.
132. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM regulation 46(2) (e), the code of conduct for councillors and the code of conduct for staff members issued in terms of the MSA.
133. Contracts and quotations were awarded to providers whose tax matters had not been declared by the South African Revenue Service to be in order, as required by SCM regulation 43.

Human resource management and compensation

134. Job descriptions were not established for all posts in which appointments were made in the current year, in contravention of section 66(1)(b) of MSA.
135. An approved staff establishment was not in place, as required by section 66(1)(a) of the MSA.
136. The competencies of chief financial officer, all financial and SCM officials were not assessed in order to identify and address gaps in competency levels as required by the Regulations on Minimum Competency Levels regulation 13.

137. The municipality did not submit a report on compliance with prescribed competency levels to the National Treasury and relevant provincial treasury as required by the Regulations on Minimum Competency Levels reg14(2)(a)
138. Senior managers did not meet any of the prescribed competency areas as required by regulation 6 and 7 of the Municipal Regulations on Minimum Competency Levels.

Asset management

139. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
140. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.
141. All investments were not made in accordance with the requirements of the investment policy, as required by Municipal investment regulation 3(3).
142. Investments were made without proper care being exercised, as required by Municipal investment regulation 5.

Liability management

143. An adequate management, accounting and information system which accounts for liabilities was not in place, as required by section 63(2)(a) of the MFMA.
144. An effective system of internal control for liabilities (including a liability register) was not in place, as required by section 63(2)(c) of the MFMA.
145. Long-term debt was incurred without a resolution of the municipal council approving the debt agreement, in contravention of section 46(2)(a) of the MFMA.

Internal control

146. I considered internal control relevant to my audit of the financial statements, Annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for disclaimer of opinion.

Leadership

147. The leadership was not able to implement effective human resource management to ensure that adequate and sufficiently skilled resources were in place, performance was monitored and consequence management was applied where necessary. This contributed to the material misstatements identified in the financial statements, the findings on predetermined objectives and non-compliance with laws and regulations.
148. In addition, the municipality did not implement and monitor the audit action plan and, as a result, numerous internal control deficiencies identified in the previous year re-curred in the current year.

Financial and performance management

149. The municipality did not prepare regular, accurate and complete financial reports, and did not perform daily and monthly processing and reconciling of transactions throughout the financial year. As a result, the municipality was unable to produce financial statements that were free from material misstatements.
150. The municipality did not have a proper record management system to ensure that complete, relevant and accurate information was accessible and available to support financial and performance reporting. This resulted in some amounts disclosed in the financial statements not being supported by relevant accounting records.
151. There were no review processes to monitor compliance with all applicable laws and regulations within the municipality. As a result, non-compliance with laws and regulations was not effectively identified or prevented and municipal officials were not held accountable for transgressions in this regard.

Governance

152. The municipality did not have adequate risk management processes in place. As a result, there were no processes to identify all risks to which the municipality was exposed and no mitigating controls were in place for the risks that had been identified.
153. The internal audit unit and the audit committee were not effective in their review of internal controls and compliance with laws and regulations. This was largely as a result of the lack of co-operation from management and capacity shortages, in terms of resources in the internal audit unit.

Auditor - General

East London

18 December 2015



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence